Office-Supreme Court, U
FILED
MAY 23 1981
ALEXANDER L. STEVA
CLERK

Nos. 80-1754 and 80-1755

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

GEORGE W. FULK, THOMAS W. SHELTON, WILLIAM F. SUDDETH, WEBSTER A. COLLINS, HERBERT R. MORRISON, HELEN O. MORRISON, AND GLEN A. WILKINSON,
Petitioners,

versus

DAVID R. JOHNSTON, THE NORTHWESTERN BANK, JAMES R. GILLEY and R. A. GILBERT,
Respondents.

In the Matter of: The Washington Group, Inc., Convenient Systems, Inc., Washington Mills Company, Johnston Mills Export Co., Spinners Processing Co., Washington Weaving Co., Washington Mills Sales Corp., Debtors.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

W. DONALD CARROLL, JR.
(Counsel of Record)
JONATHAN E. BUCHAN
Helms, Mulliss & Johnston
2800 NCNB Plaza
Charlotte, North Carolina 28280
(704) 372-9510
Attorneys for
The Northwestern Bank,
Respondent.

JOHN H. NORTHEY, III
(Counsel of Record)
Caudle, Underwood & Kinsey, P.A.
200 Civic Plaza Building
801 East Trade Street
Charlotte, North Carolina 28202
(704) 377-1200
Attorneys for
David R. Johnston,
Respondent.

TABLE OF CONTENTS

	Page
TABLE OF CASES AND AUTHORITIES	ii
OPINIONS BELOW	2
CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED	3
STATEMENT OF THE CASE	4
REASONS FOR NOT GRANTING THE WRITS	15
DISCUSSION OF REASONS FOR NOT GRANTING THE WRITS	21
CONCLUSION	61

TABLE OF CASES AND AUTHORITIES

Cases	Page
Brown v. Atwell, 92 U.S. 327 (1876)	42
Caplin v. Marine Midland Grace Trust Company, 406 U.S. 416 (1972)	17,27, 28,31, 33,36
Commercial Bank v. Buckingham's Executors, 5 How. 317, 12 L.Ed. 169 (1847)	42
Department of Motor Vehicles of the State of California v. Rios, 410 U.S. 425 (1973) . . .	42
In re Equity Funding Corp. of America, 519 F.2d 1274 (9th Cir. 1979)	38
In re Farrington Manufacturing Company, 540 F.2d 653 (4th Cir. 1976)	35,36 37
In the Matter of the Washington Group, Inc., 476 F.Supp. 246 (M.D.N.C. 1979).	3,12, 33
King v. Sharp, 63 F.R.D. 60 (N.D.Tex. 1974)	32

Cases — Page

Libby v. City National Bank, 592 F.2d 504 (9th Cir. 1978) . . 25

Matter of First Colonial Corp. of America, 544 F.2d 1291 (5th Cir.) cert. denied, 431 U.S. 904 (1977) 23

Rochelle v. Marine Midland Grace Trust Co., 535 F.2d 523 (9th Cir. 1976). 31

Triangle Improvement Council v. Ritchie, 402 U.S. 497 (1970) . 42,44

U.S. ex rel. The State of Louisiana v. Jack, 244 U.S. 397 (1917) 25

Warheit v. Osten, 57 F.R.D. 69 (E.D. Mich. 1973) 33

Statutes and Regulations

11 U.S.C. §48 (1953) 22

11 U.S.C. §67(c) (1968) 23

11 U.S.C. §589 (1976) 46

11 U.S.C. § 1108 (Supp. III 1979) . 46

29 U.S.C. §1002(21) (1976). 20,46 49

29 U.S.C. §1031 (1976). 3,47

	Page
29 U.S.C. §1105 (1976).	46
29 U.S.C. §1132 (1976).	54
29 U.S.C. §1137(b) (1976)	3,47
29 U.S.C. §1144(d) (1976)	3,18 47
Sup.Ct.R. 17 (1980)	40,41
Sup.Ct.R. 34 (1980)	46
Fed.R.App.P. 4	23,24
Fed.R.App.P. 6	23
Fed.R.Bank.P. 806	55
Fed.R.Bank.P. 10-208.	57
Miscellaneous	
Collier Bankruptcy Manual, §25.02[2] (2d.Ed.	23
Moore, Federal Practice, (Vol. 9, ¶203.06) (2d.Ed. 1975).	24

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1980

Nos. 80-1754 and 80-1755

GEORGE W. FULK, THOMAS W. SHELTON, WILLIAM F. SUDDETH, WEBSTER A. COLLINS, HERBERT R. MORRISON, HELEN O. MORRISON, AND GLEN A. WILKINSON,

Petitioners,

versus

DAVID R. JOHNSTON, THE NORTHWESTERN BANK, JAMES R. GILLEY and R. A. GILBERT,

Respondents.

In the Matter of: The Washington Group, Inc., Convenient Systems, Inc., Washington Mills Company, Johnston Mills Export Co., Spinners Processing Co., Washington Weaving Co., Washington Mills Sales Corp., Debtors.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Respondents respectfully pray the Court to deny both: (1) the petition of Webster A. Collins, Herbert R. Morrison, Helen O. Morrison and Glen A. Wilkinson ("Collins Petition") seeking a writ of certiorari to review the judgment of the United States Court of Appeals for the Fourth Circuit in this case; and (2) the separate petition of George W. Fulk, Thomas W. Shelton and William F. Suddeth ("Fulk Petition") seeking a similar writ.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Fourth Circuit has not been reported. It is reprinted in the appendices to both the Fulk and the Collins petitions. The opinion of the United States District Court for the Middle District of North Carolina

is reported at 476 F.Supp. 246 (M.D.N.C. 1979). It is reproduced in the appendices to both the Fulk and the Collins petitions. Petitioners' appendices contain various other orders of the courts below, and these are not reproduced again here. Both petitions omit reference to or reproduction of the May 15, 1980 opinion of the bankruptcy court below and that opinion is attached as Appendix A to this brief.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

In addition to the statutory provisions referred to in the Fulk petition and the Collins petition, sections 514(d), 111, and 507(b) of the Employee Retirement Income Security Act of 1974, 29 U.S.C. §1144(d), 1031 and 1137(b) are relevant. These

provisions are set forth in Appendix B hereto.

STATEMENT OF THE CASE

On January 15, 1979, R. A. Gilbert, trustee of the Washington Group, Inc., Convenient Systems, Inc., Washington Mills Company, Johnston Mills Company, Johnston Mills Export Company, Spinners Processing Company, Washington Weaving Company, and Washington Sales Corporation (hereinafter referred to as "Debtors"), in a Chapter X reorganization proceeding, filed an application in the Bankruptcy Court requesting an order authorizing him to expend funds of the debtors to pay expenses incurred in the prosecution of two alleged class actions: Collins, et al. v. Bagley, et al., civil action

number C-78-335-WS (M.D.N.C.) and Fulk, et al. v. Bagley, et al., civil action number C-78-333-WS (M.D.N.C.).

The bankruptcy court issued an ex parte order dated January 16, 1979 (hereinafter referred to as "January 16, 1979 order") authorizing the expenditure of the debtors' funds for the purpose of paying the expenses of an uncertified group of alleged participants in terminated employee benefit plans of the Washington Group, Inc. in Fulk. No notice of the application or order was given by the bankruptcy court or by trustee R. A. Gilbert, to any creditor or to any shareholder of the debtors.

Respondent David R. Johnston is a shareholder of the debtors and at the time of entry of the order in question

respondent James R. Gilley was majority shareholder of the debtors[1]. Respondents The Northwestern Bank and Johnston are creditors of record of the debtors in the reorganization proceeding. The trustee of the debtors, while joined with the petitioners in the initial appeal to the Fourth Circuit Court of Appeals, has not joined with the petitioners in seeking a writ of certiorari, although he has filed a brief in support of the Fulk petition.

1/ When this case was argued in the Fourth Circuit, Gilley's attorney represented to that court that Gilley had sold his stock in the debtors and no longer had an interest in this litigation.

The application for entry of the bankruptcy court's ex parte funding order came at a critical time in the development of the two lawsuits it was designed to assist.

Collins, et al. v. Bagley, et al. is principally an action by an alleged class of shareholders asserted under the federal securities laws and certain state laws. The Collins suit as originally brought included separate claims by the trustee seeking to recover on behalf of the debtors from certain individuals for alleged corporate mismanagement. The trustee is presently seeking to have his action severed from that of the alleged class of shareholders and the question of misjoinder is currently pending before the district court. No issue

concerning the trustee's individual claims has been raised in the appeal or is raised here.

Fulk, et al. v. Bagley, et al. is an action brought by the chairman of the administrative committees of certain employee benefit plans of the debtors in his capacity as a fiduciary and also by a purported class of employees and former employees of the debtors claiming vested or contingent interests under certain terminated employee benefit plans. The Fulk suit asserts claims principally under the Employee Retirement Income Security Act (ERISA) and the federal securities laws.

Both these actions were filed on July 26, 1978. The purported class action plaintiffs in each suit --

represented by the same set of law firms -- are the individuals who have filed the petitions for certiorari in this Court.

On November 6, 1978, District Judge Eugene A. Gordon entered an order establishing an orderly procedure for the handling of the Collins and Fulk cases. These orders directed initial discovery in the two cases to proceed only on the question of class certification. Discovery concerning the class question has now been completed and the issue of the propriety of class certification is pending before the district court.

The class action discovery raised serious questions concerning the adequacy of the named "representative plaintiffs." Discovery in the Collins

case in November and December, 1978 revealed that those named plaintiffs had limited their financial commitment and had agreed to pay only a small fraction of the expected costs of that action.[2] Class action discovery in

---

2/ Discovery also revealed other problems with the named plaintiffs in Collins. For example, on November 24, 1978, counsel for plaintiffs in Collins filed a class action certification brief asserting that Douglas B. Collins, one of the named plaintiffs obligated to pay the costs of this action, was an adequate, competent and proper class representative "familiar with the underlying facts in this litigation" and "participating with and assisting counsel." On December 8, 1978, after defendants noticed the deposition of Douglas B. Collins, plaintiffs' counsel filed an affidavit stating that Douglas Collins was "incapable of making full business-type judgments or using normal logic to meet every-day problems," that his father and his brother "have handled all legal and business affairs for Douglas Collins" and that "he would be unable to fulfill any of the obligations of a class representative."

the Fulk case revealed that the purported class representatives had met with their lawyers for the first time on July 24, 1978, two days before the twenty-page complaint naming them as class representatives was filed. George Fulk testified that at the time he selected the named plaintiffs more than six months before entry of the bankruptcy court's January 16, 1979 funding order he informed those employees that the expenses of the proposed class action suit to which they were to lend their names would be paid for by the trustee for the debtors.

When these questions surfaced concerning the adequacy of the class plaintiffs -- in terms of their willingness and ability to bear the

expense of the suits as well as otherwise -- the trustee sought and obtained the ex parte order from the bankruptcy court authorizing the expenditure of funds from the debtors' estates to finance the costs of the two alleged class actions. Creditors and shareholders in the reorganization proceeding appealed from that order to the United States District Court. None of the petitioners here were parties to that appeal. On September 5, 1979 the district court filed an order and memorandum of decision, finding that the bankruptcy judge had erred in allowing the trustee to expend funds of the debtors' estates to assist in bearing the cost of "two potentially massive civil suits." 476 F.Supp. 246, 247, (Fulk Petition Appendix B, p. 4a)

Thereafter, on September 14, 1979, each set of purported class plaintiffs, petitioners herein, filed with the bankruptcy court documents purporting to be proofs of claims of the uncertified classes in the Collins and Fulk suits against the debtors' estates. The tendered proofs of claims incorporated by reference the entire complaints in the Collins and Fulk actions and asserted that the reorganization trustee was liable to the respective alleged class claimants in the full amounts they sought in those two suits.

On that same date the purported class plaintiffs filed objections to the approval of plans of reorganization the bankruptcy court was then considering as a way to

relieve the financial condition of the debtors. On October 2, 1979 the purported class plaintiffs entered for the first time the proceedings arising out of the challenged January 16, 1979 order by filing a notice of appeal from the district court's September 5, 1979 order.

On May 15, 1980, the bankruptcy judge who entered the January 16, 1979 order addressed, in a ruling on a related matter, his unwillingness to allow the expenditure of funds from the debtors' estates to pay expenses incurred in the prosecution of class action activities in Collins and Fulk. (That order, not included in the appendices to petitioners' petitions, is attached as Appendix A to this brief.) The bankruptcy judge stated in his opinion:

> If the circumstances and the facts concerning these suits now known to this Court had been known at the time application for authority to expend funds for costs in these plenary class actions was made, this Court would never have entered the January 16, 1979 Order allowing such expenditures.
>
> . . . the so-called class claims and actions by Collins and Shelton-Fulk which are the basis of the alleged claims before this Court are being pursued for the benefit of the attorneys rather than for the benefit of their so-called plaintiffs and clients. (Appendix A, pp. 25a, 37a, Emphasis added.)

Thus, the judge who entered the initial funding order without notice or hearing determined, upon learning more of the relevant facts, that entry of such a funding order should not have occurred.

REASONS FOR NOT GRANTING THE WRITS

Petitioners' request for a writ of certiorari should not be granted

for, among others, the following reasons:

1. The petitioners have no right to present an issue for review in this Court because:

   (a) they were not parties to the initial proceeding before the bankruptcy court in which the January 16, 1979 Order in question was entered;

   (b) they were not parties to the proceeding on appeal to the district court in which the district court reviewed on the record the bankruptcy judge's order on appeal.

2. The controlling principles applicable to the Fulk petition and to the Collins petition were recently articulated by this Court in Caplin vs. Marine Midland Grace Trust Company, 406 U.S. 416, 92 S.Ct. 1678, 32 L.Ed. 2d 195 (1972). No court of appeals has held that the Employee Retirement Income Security Act of 1974 ("ERISA") modifies the obligations of a reorganization trustee under the Bankruptcy Act and there is no split in decisional authority in the circuit courts.

3. The argument presented in the Fulk petition that ERISA modified the Bankruptcy Act was not presented, argued or decided below and is, therefore, not properly before this Court as a basis for allowing a writ for certiorari.

4. The Fulk petitioners' assertion that their petition should be granted because ERISA modifies the duties of the trustee under the Bankruptcy Act is untenable because ERISA specifically provides, in 29 U.S.C. §1144(d), that ERISA in no way modifies or alters other federal statutes such as the Bankruptcy Act.

5. The record is devoid of facts or legal authority to support the Fulk petitioners' assertion that the reorganization trustee is not only a trustee for the debtors' estates, but is also saddled with conflicting trust obligations pursuant to ERISA. All of the employee benefit plans here at issue were terminated and their assets distributed or transferred to the Pension Benefit Guaranty Corporation prior to the entry of the January 16, 1979 funding order, and the reorganization trustee

never held any assets of any employee benefit plan. Thus, even assuming arguendo that ERISA somehow modified the Bankruptcy Act, the reorganization trustee does not meet the definition of a fiduciary set forth in ERISA, 29 U.S.C. §1002(21).

6. The record before the bankruptcy court and the record before the district court, as specified under Rule 806 of the Rules of Bankruptcy Procedure, provided no factual support for entry of the January 16, 1979 funding order and the order was, therefore properly reversed by the

district court and that reversal was properly affirmed by the Fourth Circuit Court of Appeals.

DISCUSSION OF REASONS
FOR NOT GRANTING THE WRITS

1. The petitioners have no rights to seek this review because they were not parties to the initial proceeding before the bankruptcy court which issued the January 16, 1979 order and because they were not parties to the proceeding on appeal before the district court and were not aggrieved by the entry of the September 5, 1979 order reversing the bankruptcy court's January 16, 1979 order.

The reorganization trustee participated in the initial proceedings below and the subsequent proceedings through the initial decision of the Fourth Circuit Court of Appeals, affirming the district

court's order, but did not petition this Court for review. The petitioners here were strangers to this appeal until after the September 5, 1979 order of the district court reversing the bankruptcy judge's order of January 16, 1979. Petitioners had not participated in any manner in the proceedings in the bankruptcy court, nor had they made any appearance or played any role in the proceedings before the district court prior to its September 5, 1979 order.

Until 1968 appeals from bankruptcy proceedings were governed by former §25(a) of the Bankruptcy Act, 11 U.S.C. §48 which provided: "Appeals from this act to the United States Court of Appeals shall be taken within thirty (30) days after written notice

to the aggrieved party of the entry of judgment . . . ." (Emphasis added.) In 1968, §25(a) of the Bankruptcy Act was superseded by Rules 4 and 6 of the Federal Rules of Appellate Procedure. Collier Bankruptcy Manual, §25.02[2] at p.317 (2d Ed.).[3] Rule 4 likewise provides that it is a party to a civil action in a district court, including a proceeding in bankruptcy or controversy arising therein, who may appeal to the court of appeals.

3/ The present section providing for appeals to the district court from the bankruptcy court, provides that a "person aggrieved" may appeal from an order of a bankruptcy judge to a district court. Bankruptcy Act, §39(c), 11 U.S.C. §67(c) (1968). The group (i.e. "persons") who can appeal from orders of the bankruptcy judge is therefore broader than the group (i.e.) "parties") who can appeal to the court of appeals. Matter of First Colonial Corp. of America, 544 F.2d 1291 (5th Cir.) cert. denied, 431 U.S. 904 (1977).

The rule that only a party to a proceeding below may appeal is well established in the federal courts:

> Ordinarily only a person who was a party in the Court below and who is aggrieved by the judgment or order can appeal therefrom. 9 J. Moore, Federal Practice ¶203.06 at p.715 (2d Ed. 1975).

The Fourth Circuit Court of Appeals was not required to address the issue of petitioners' right to participate for the first time at the circuit court level since the trustee was a party to the proceedings in the bankruptcy court and the district court and since he also participated in the appeal to the circuit court. However, the trustee is not seeking additional review here and the petitioners - who were not parties in the proceedings before the district court -- are not, under Rule 4, parties

who can seek review here. U.S. ex rel. The State of Louisiana v. Jack, 244 U.S. 397, 37 S.Ct. 368, 61 L.Ed. 1222 (1917).

Not only must petitioners have been parties to the proceeding before the district court, they must also have been "aggrieved" by the district court's decision in order to seek review in the circuit court and, consequently, to seek review here. The federal courts have held that in order to appeal the ruling of a court in a civil action, the party seeking to appeal must have an interest which is "immediate and pecuniary and not a remote consequence of the judgment". Libby v. City National Bank, 592 F.2d 504, 511 (9th Cir. 1978).

Petitioners are identified in the petition only as either present and former employees of the debtors and plaintiffs in Fulk or stockholders of the debtor corporations and plaintiffs in Collins. Petitioners do not, as would-be participants in the proceedings designed to reorganize the debtors, assert any direct and immediate interest they may have in the issue of whether the trustee can be allowed to fund the prosecution of the Collins and the Fulk actions. The interests these petitioners have in the outcome of that issue relate not to any interests they have as participants in the reorganization proceeding but only to their interests as plaintiffs in the two civil suits in that if the trustee is allowed to fund

these two third-party suits, the alleged "class representatives" will be able to avoid making any financial commitment to the actions. The fact that resolution of this issue has some consequential effects on petitioners in a collateral proceeding does not give them the right to intervene on appeal as an "aggrieved party".

Petitioners, therefore, were not "parties" to the orders of the bankruptcy and district courts and are not, in any event, "aggrieved" as would-be participants in the reorganization proceeding.

2. The controlling principles applicable to this case were recently articulated by this Court in Caplin v. Marine Midland Grace Trust Co., 406 U.S. 416, 92 S.Ct. 1678, 32 L.Ed. 2d 195 (1972). There is no split in decisional authority in the circuit courts.

The decisions of the bankruptcy and district courts in this case are consistent with the rationale of this Court's decision in Caplin v. Marine Midland Grace Trust Co., 406 U.S. 416, 92 S.Ct. 1678, 32 L.Ed. 2d 195 (1972), and other lower federal courts have applied Caplin the same way.

In Caplin, a corporation involved in real estate activities delivered an indenture to Marine Midland Grace Trust Company to secure the corporation's issue of debentures of a total value of approximately $8.6 million. In the indenture, the corporation agreed to maintain a two-to-one ratio of assets to liabilities to protect the investments of the debenture holders. After the corporation suffered losses for

several successive years, Marine Midland petitioned for the reorganization of the corporation under Chapter X of the Bankruptcy Act. The trustee appointed by the court found after investigation that the corporation had assets of approximately $21.5 million and liabilities of about $60 million, including approximately $4.3 million in outstanding debentures. Investigation also led the trustee to conclude that Marine Midland, the indenture trustee, had either willfully or negligently failed to fulfill its obligations under the indenture, in that it had permitted the corporation fraudulently to issue certificates showing compliance with the required ratio.

After concluding his investigation, the trustee filed an independent action on behalf of debenture holders against Marine Midland seeking to recover the principal amount of the outstanding debentures as damages for Marine Midland's alleged bad faith failure to compel the corporation's compliance with the terms of the indenture. This Court held that the trustee had no standing in his capacity as a trustee in a Chapter X reorganization to pursue claims on behalf of the debenture holders against Marine Midland. This Court squarely addressed and rejected the trustee's argument that the trustee was the proper party to take corrective action in such a situation. This Court stated that the statutory

scheme setting forth the powers of the reorganization trustee nowhere grants the trustee authority to prosecute legal actions on behalf of third parties to the reorganization proceeding. The Court noted that a change giving the reorganization trustee such powers was a policy decision to be made by Congress, not by the Court. Congress has to date refused the invitation to change that policy.

In Rochelle v. Marine Midland Grace Trust Co., 535 F.2d 523, (9th Cir. 1976), the Ninth Circuit upheld the dismissal of the securities law claims asserted on behalf of Sunset's creditors and debenture holders by the reorganization trustee of Sunset, the debtor corporation. Citing Caplin, the Ninth Circuit held that the

reorganization trustee had no standing to maintain an action on behalf of any person or entity other than the debtor corporation. 535 F.2d 523, 527 (1976).

In King v. Sharp, 63 F.R.D. 60 (N.D.Tex. 1974), the court refused to certify a class action in which a trustee in a Chapter X proceeding sought to represent a class in an action under the securities laws against defendants, who had control of the company prior to the bankruptcy petition. The court there based its decision on two determinations:

1. That the bankruptcy laws do not authorize the trustee to "champion causes" for the purpose of benefiting third parties; and

2. That a conflict was inherent in such representation since no direct benefit would accrue to the bankrupt estate from the expenditures of the funds of the estate.

Similarly in Warheit v. Osten, 57 F.R.D. 629 (E.D. Mich. 1973) the district court denied a Chapter XI receiver's motion for intervention in a securities action on the ground that the receiver did not have standing to sue on behalf of stockholders or others to enforce their claims.

As the district court below noted in its decision in this case, petitioners are:

> asking this Court to limit Caplin to cases where the Trustee actually is suing on behalf of some third party claimant as opposed to cases where the trustee is merely footing the bill [and] requesting the Court to allow [the Trustee] to do indirectly what Caplin forbids his doing directly.

476 F.Supp. 246, 252 (1979). (Fulk Petition, Appendix B, p. 14a).

The district court below recognized that the trustee in the

reorganization is not favorably positioned to decide which of many legal actions available to third parties may have some possible effect on the debtor's estate. Moreover, because the trustee is a fiduciary as to the debtor's estate, he cannot undertake the additional fiduciary duties inherent in funding a class action which may conflict with his primary obligations under the Bankruptcy Act. In this case the petitioners irreparably created such a conflict several days after the district court's decision when they filed claims against the trustee for damages for the identical alleged wrongdoing they alleged in the two purported class actions whose prosecution they are seeking to have the trustee fund.

The Fourth Circuit's decision in In re Farrington Manufacturing Company, 540 F.2d 653 (4th Cir. 1976), which was discussed in the briefs of both parties in the circuit court, does not help petitioners. Farrington involved a dispute over the allowance of fees to the trustee's legal counsel after the services for which the fees were sought had been rendered. The former trustee and his attorneys appealed the amount of the allowance of attorney's fees allowed by the district court on the ground that they were too low. The former trustee had assisted indirectly (not funded) the prosecution of a suit brought on behalf of debenture holders of the debtor corporation. The Fourth Circuit, in reversing the district court's ruling

and allowing a greater amount, considered the time spent by the attorneys for the trustee in assisting the trustee and other parties to that action. It appears from the opinion that the Fourth Circuit was deeply concerned about the trustee's limited participation in the debenture holders' suit in light of the Caplin decision.

It is important to note that the issue presented in Farrington is not the issue presented on this appeal. Farrington involved reimbursement for expenses and compensation for services rendered by the trustee or his attorney in consulting with someone involved in another lawsuit. In the instant case, what the district court below found improper--and what shareholders and

creditors object to and find unsupportable--is the "blank check" aspect of this pre-authorized payment from the funds of the estate, to attorneys not representing the trustee, for the expenses in maintaining two class actions on behalf of the third parties.

Petitioners' suggest that the courts below "ignored the Fourth Circuit's own decision in Farrington." (Fulk petition, p. 9; see Collins petition, p. 15, fn. 21.) The relevance of Farrington was discussed in the briefs submitted to the district court and to the court of appeals. The Fourth Circuit affirmed the district court's decision in a per curiam opinion and denied a request for a rehearing and a rehearing en banc.

(Collins Petition, Appendix I, p.27a.) The Fourth Circuit did not ignore or misinterpret its own prior decision.

The decision of the Fourth Circuit in this case is not in conflict with the Ninth Circuit's decision in In re Equity Funding Corp. of America, 519 F.2d 1274 (9th Cir. 1979) relied upon by petitioners. In fact, the issues decided in Equity Funding are wholly different from the issues petitioners seek to raise here. Equity Funding concerned the scope of the district court's discretion in authorizing a reorganization trustee to enter into a settlement agreement. The facts from which the Equity Funding case arose are somewhat complex and perhaps unique since when Equity went into a Chapter X reorganization proceeding, one of the

wholly owned subsidiaries, as an insurance company, remained outside the jurisdiction of the federal bankruptcy action. The subsidiary was subject to a liquidation proceeding under state law. The trustee for the debtor corporation had claims asserted against it related to the wholly-owned insurance subsidiary. In addition, the trustee himself had claims against the subsidiary. Allegedly defrauded shareholders also had claims in the Illinois liquidation proceeding. In resolving those numerous claims the bankruptcy trustee participated in a settlement agreement to which all of these entities were parties; the trustee received approval from the court for that settlement. The terms of the settlement included the setting

aside of a fund by the director of the state liquidation proceeding to be used to pay legal fees in both the Illinois liquidation proceeding and in separate proceedings which had been consolidated in one multi-district litigation forum. All of the settlement proceeds channeled to the trustee and to the defrauded claimants derived from the Illinois state liquidation proceeding.

At no time in that case was the question presented whether a reorganization trustee has authority to fund litigation on behalf of third parties, and there is no holding to that effect in that case. In summary, petitioners have failed to present a case from any other circuit conflicting with the decision of the

Fourth Circuit Court of Appeals below. See Supreme Court Rule 17.1(a).

3. The argument presented in the Fulk Petition that the Employee Retirement Income Security Act (ERISA) modified the Bankruptcy Act was not presented, argued or decided below and is, therefore, not properly before this court as a reason to allow a petition for certiorari.

Rule 17.1 of the Rules of the United States Supreme Court provides that one basis for granting a petition for a writ of certiorari is that a federal court of appeals has decided an important question of federal law which has not been, but which should be, settled by the Supreme Court. As the record in this case manifests, the issue of whether ERISA has modified the Bankruptcy Act was not presented, argued or decided in the bankruptcy

court, in the district court or in the Fourth Circuit Court of Appeals. Thus, this is not a case in which a question of federal law not settled by the Supreme Court has been decided below.

This Court has also indicated that before a petition of writ of certiorari can be granted, it must be apparent that a federal question was raised and decided "in order to induce the judgment" below. Commercial Bank v. Buckingham's Executors, 5 How. 317, 341, 12 L.Ed. 169 (1847), cited in Department of Motor Vehicles of the State of California v. Rios, 410 U.S. 425, 93 S.Ct. 1019, 35 L.Ed.2d 398 (1973). See also Brown v. Atwell, 92 U.S. 327, 23 L.Ed. 511 (1876).

In Triangle Improvement Council v. Ritchie, 402 U.S. 497, 91 S.Ct.

1650, 29 L.Ed.2d 61 (1970), this Court dismissed a writ of certiorari as improvidently granted. The Court summarized the factual situation as follows: After the writ of certiorari was granted, the statute upon which the petitioners based their case had been repealed and a new statute had been enacted by Congress, altering the impact of any decision the Court might make on the merits. The Court also noted that the petitioners in their brief on the merits in the Supreme Court had "almost completely abandoned their original claim for relief" and sought to broaden substantially the nature of the remedy they were seeking.

In dismissing the writ, the Court stated:

> It is troublesome that the petitioners have virtually abandoned their initial claim for relief. Instead of the preparation of a plan, they now seek a decree that the district court should bring before it all persons displaced by the highway and inquire whether their new locations meets statutory standards. As to this issue, there is neither an opinion below nor a record upon which to judge the claim. [Emphasis added.]

The Court noted that in light of the change in posture of the case, its adjudication would not be a "provident expenditure of the energies of the Court." 402 U.S. 497, 501-502, 91 S.Ct. 1650, 1352, 29 L.Ed. 2d 61 (1970).

The absence of presentation or discussion of this issue or a ruling on this issue below warrants a denial of this petition.

4. The Fulk petitioners' assertion that their petition should be granted because of the modification

> by ERISA of the duties of the trustee under the Bankruptcy Act is untenable because ERISA specifically provides in 29 U.S.C. 1144(d) that ERISA in no way modifies or alters other Federal statutes such as the Bankruptcy Act.

The primary thrust of the Fulk petition is that the district and circuit courts failed to harmonize "the interaction of the Bankruptcy Act and the Employee Retirement Income Security Act of 1974." (Fulk Petition, p. 8) Strikingly, the Fulk petition nowhere indicates what provision of either the Bankruptcy Act or ERISA allows a reorganization trustee to fund third-party lawsuits. Having failed to identify any provision of these statutes authorizing such action, the petition also fails to identify the purported conflict or to

specify the precise section of either statute to which the petition claims the lower court gave an "unduly restrictive interpretation." This omission is not happenstance; there is no conflict.

As required by Rule 34 of the Supreme Court Rules, both petitions have designated certain statutory provisions as being involved here. In the Fulk petition, these are designated as §3(21) and §405 of the Employee Retirement Income Security Act of 1974, 29 U.S.C. §1002(21) and §1105, and §189 of the Bankruptcy Act, 11 U.S.C. §589, recodified as 11 U.S.C. §1108 (Supp. III 1979). These provisions are set forth in the appendix to the Fulk petition. A close examination of the terms of each of

these sections shows that they provide no authority for the suggestion that the trustee is empowered to expend funds of the debtors to defray the costs of third-party litigation.

There is no dispute that the Bankruptcy Act is devoid of any authorization for the trustee to expend the debtors' funds in this fashion. Nonetheless, the Fulk petition argues that the enactment of ERISA somehow increased the authority of the trustee under the Bankruptcy Act to engage in such activities. However, even if the language of ERISA can be read to imply such an intent, which it clearly cannot, ERISA expressly provides in §1144(d) that:

> Nothing in this subchapter shall be construed to alter, amend, modify, invalidate, impair or supersede any law of the United States except as provided in

> §1031 and 1137(b) or any rule or regulation issued under any such law.

The exceptions in §1031 relate to the repeal of the Welfare and Pension Plans Disclosure Act and in §1137(b) to employee benefit plans which cover employees of the United States. Neither exception is applicable here. Thus, the Fulk petitioners' argument that ERISA somehow modifies the Bankruptcy Act flies squarely in the face of the express language of ERISA itself.

> 5. The record is devoid of facts or legal authority to support the Fulk petitioners' assertion that the reorganization trustee is not only a trustee for the debtors' estates, but is also saddled with conflicting trust obligations pursuant to ERISA.

As is set forth above, there is no

legal authority for the Fulk petitioners' argument that enactment of ERISA changed the obligations of the reorganization trustee in Chapter X proceedings. Moreover, there are no facts in this record to sustain the position that the reorganization trustee is a "fiduciary" under the provisions of ERISA. ERISA defines a fiduciary as one who exercises discretionary authority with regard to an employee benefit plan or plan assets or who renders investment advice or who has discretionary responsibility for the administration of the plan. 29 U.S.C. §1002(21).

The employee benefit plans here at issue consist principally of three types: a stock purchase plan, an employee pension plan, and three

employee profit sharing plans. No contributions to the employee pension benefit plan were made after early 1976. After the debtors filed for reorganization, administration of the assets was turned over to the Pension Benefit Guaranty Corporation. The profit sharing plans were terminated in 1976 and the assets of those plans were disbursed to the beneficiaries of the plans months prior to the June 1977 filing of the reorganization proceeding and years before the January 16, 1979 funding order was entered. The employee stock purchase plan was terminated prior to the commencement of the bankruptcy reorganization and the assets of that plan were all returned to the plan beneficiaries. Thus, the

reorganization trustee has held no employee benefit plan assets, has had no occasion to give investment advice and has administered no plan activities.

Without question, even if ERISA, contrary to the terms of the act itself, had sought to modify the trustee's powers under the Bankruptcy Act, such modificiation would not, under the facts in this record, clothe the reorganization trustee with additional fiduciary duties under ERISA.

There are strong policy reasons for not burdening the reorganization trustee with additional responsibilities under ERISA. To do so would put the trustee in conflict with his primary obligations to the

debtor's estate and to the creditors of the debtor. A trustee cannot have conflicting trust obligations and properly serve either the estates or employee plans as a trustee. Expenditure of trust funds for employee benefit plan participants conflicts with the interest of creditors in maintaining the assets of the estate. An identical problem is created by the trustee's support of lawsuits brought on behalf of the shareholders. Expenditure of funds for the benefit of shareholders places the subordinate interests of the shareholders in conflict with the interests of creditors which occupy a higher position under the Bankruptcy Act's priority rules.

That conflict is particularly striking on the facts of this record. The shareholders and employee benefit plan claimants seeking to have the trustee fund their purported class actions have subsequently turned on the trustee and have brought claims against him for the same alleged wrongs. The trustee is thus being asked to spend the debtors' funds on actions on behalf of third parties at the same time he is required to spend the debtors' funds resisting the very same claims being made against him.

The Fulk petition suggests that it is important to have the trustee fund the alleged class plaintiffs in the Fulk suit since these class plaintiffs are otherwise without means to maintain a class action. However,

that suit is also brought by Fulk in his individual capacity as chairman of the plan committees for the employee benefit plans and an alleged fiduciary for the employees. Outside funding of that suit is not required to enable him to litigate an action to recover on behalf of all beneficiaries of the employee benefit plan. Indeed, under the liberal provisions of ERISA, any fiduciary of the plan, any participant thereof, or the Secretary of Labor may bring a civil action to recover benefits due participants under the plans. 29 U.S.C. §1132.

In regard to the Collins action, it is apparent that the reason for seeking funding from the trustee was to provide a way to bolster the deficiences of the purported class

plaintiffs who, in the words of the bankruptcy judge, "are no more than 'straw claimants'" and whose "claims are made on behalf of the attorneys, not a valid certifiable group of class claimants." (Appendix A, p. 37a)

The question of the trustee's authority to fund third-party actions should not be reached because this record does not contain facts which would justify such expenditures even if such authority did, in fact, exist.

6. The record before the Bankruptcy Court and the record before the District Court, as specified under Rule 806 of the Rules of Bankruptcy Procedure, provided no factual support for entry of the January 16, 1979 Funding Order and the Order was, therefore, properly reversed by the District Court and that reversal properly affirmed by the Fourth Circuit Court of Appeals.

The record before the bankruptcy court and the record before the district court as specified under Rule 806 of the Rules of Bankruptcy Procedure provided no support for the entry for the January 16, 1979 funding order.

At the time the January 16, 1979 order was entered, the bankruptcy court had before it no sworn evidence which even purported to justify the order. Nor was there any evidence before the district court supporting the bankruptcy court's order at the time the district court rendered its decision disallowing that order.

The January 16, 1979 order recites in its preamble the following:

> The Court having found as facts the matters raised in said application....

However, that bare recitation is not supported by any factual record because: (1) the trustee's application was unsworn and consists largely of conclusory allegations; and (2) as the order itself demonstrated, no hearing was held by the bankruptcy court to take evidence on the trustee's request. The trustee's Rule 10-208 report of his ex parte investigation was never the subject of cross-examination by any parties in the Chapter X proceedings. Although that report was included at appellants' request in the appendix filed with the court below, it was not a part of the record on appeal to the district court, it is not sworn to, and it does not provide competent evidence to support the bankruptcy court's order.

After Fulk et al. and Collins et al. filed their claims in the reorganization proceedings, the bankruptcy court was given an opportunity to learn more about the facts surrounding the two actions then pending in the district court and the circumstances leading up to the January 16, 1979 funding order. On May 15, 1980 the same bankruptcy judge who had entered the January 16, 1979 funding order entered another order, addressing the bankruptcy court's unwillingness to allow the expenditure of funds from the debtors' estates to pay expenses incurred in the prosecution of class action activities in Collins and Fulk. The bankruptcy judge stated in that opinion that if the circumstances and facts concerning

these suits now known to the court had been known at the time application for authority to expend funds for costs was made, he would have never entered the January 16, 1979 order allowing such expenditures.

The bankruptcy judge's May 15, 1980 opinion--made after he had learned more about the circumstances surrounding the litigation and the attempts to obtain funding from the trustee, and not made merely as a result of an ex parte application--underscores the motivation behind petitioners' efforts to have the debtors fund the costs of their two suits.

In essence, all of the asserted "facts" petitioners discussed at length as the basis for the bankruptcy

court's order are not judicially-found facts at all, but are mere unsupported contentions of the purported class plaintiffs in the Collins and Fulk lawsuits.

CONCLUSION

For the reasons set forth above, this Court should deny the petitions for writ of certiorari to review the judgment of the Court of Appeals in the Fourth Circuit.

Respectfully submitted,

W. Donald Carroll, Jr.
(Counsel of Record)
Jonathan E. Buchan
Helms, Mulliss & Johnston
2800 NCNB Plaza
Charlotte, N. C. 28280
(704) 372-9510
Attorneys for
The Northwestern Bank,
Respondent.

John H. Northey, III
(Counsel of Record)
Caudle, Underwood &
Kinsey, P.A.
200 Civic Plaza Building
801 East Trade Street
Charlotte, N. C. 28202
(704) 377-1200
Attorneys for
David R. Johnston,
Respondent.

APPENDICES

APPENDIX A

UNITED STATES BANKRUPTCY COURT
FOR THE MIDDLE DISTRICT OF
NORTH CAROLINA

IN THE MATTER OF:	)	
THE WASHINGTON GROUP, INC.; CONVENIENT SYSTEMS, INC.; WASHINGTON MILLS COMPANY; JOHNSTON MILLS COMPANY; JOHNSTON MILLS EXPORT COMPANY; SPINNERS PROCESSING COMPANY; WASHINGTON WEAVING COMPANY and WASHINGTON MILLS SALES CORPORATION,	)	IN CHAPTER X REORGANIZATION NUMBERS B-77-695, B-77-696, B-77-697, B-77-698, B-77-699, B-77-700, B-77-701, & B-77-702
Debtors.	)	

MEMORANDUM OPINION

This Memorandum Opinion is pursuant to a hearing on the following matters:

1. Application by Webster A. Collins, Herbert R. Morrison, Helen O. Morrison, W. O. Gregory and Glen A. Wilkinson to amend the Trustee's list of creditors to include

similarly situated defrauded investors, shareholders and former shareholders of the Washington Group, Inc. as set forth in the proof of multiple claims filed simultaneously with this application. (hereinafter referred to as the Collins shareholders' class claim.) This application also included a request to require notice to all potential class claimants similarly situated. This application and proof of multiple claim was filed on September 14, 1979 for $15,590,000.

2. Application by Thomas W. Shelton, William F. Suddeth and George W. Fulk to amend the Trustee's list of creditors to include all similarly situated employees of the debtors holding claims against the debtors as set forth in the proof of multiple claims filed simultaneously with this application for $2,800,000. (Here-

inafter referred to as the Shelton-Fulk employees' class claim.) This application also included a request that the class applicants receive notice of all matters pertaining to the bankruptcy proceedings. This application was filed on September 14, 1979.

3. Supplement to application of Webster A. Collins, Herbert R. Morrison, Helen O. Morrison, W. O. Gregory and Glen A. Wilkinson to amend the Trustee's list of creditors and to require notice as filed by the Collins shareholders' class claimants. This was filed on November 2, 1979.

4. Supplement to application by Thomas W. Shelton, William F. Suddeth, and George W. Fulk to amend the Trustee's list of creditors and to require notice as filed by the Shelton-Fulk employees'

class claimants. This supplement was filed on November 2, 1979.

5. Motion by A. M. Pullen to strike and dismiss application by Collins, et al. to amend Trustee's list of creditors and motion to dismiss objection to claim of A. M. Pullen, filed by Collins, et al. This motion was filed on December 17, 1979.

6. Motion by A. M. Pullen to strike and dismiss application by Shelton, et al. to amend Trustee's list of creditors and motion to strike and dismiss objection to claim of A. M. Pullen, filed by Shelton, et al. This motion was filed on December 17, 1979.

7. Motion by Calcott, Ltd. to strike and dismiss application to amend Trustee's list of creditors filed by Collins, Morrison, Morrison, Gregory, Wilkinson, Shelton, Suddeth and Fulk. This motion was filed on February 27, 1980.

8. Opposition of Northwestern Bank to application by Collins, et al. and Shelton, et al. to amend Trustee's list of creditors and to require notice. This document was filed on October 25, 1979.

9. Response of Trustee to the applications of Collins, et al. and Shelton, et al. to amend Trustee's list of creditors and objection of Trustee to proofs of multiple claims. This response was filed on November 5, 1979.

10. Objections by Collins shareholder class claimants to the below listed claims:

a. American Bank and Trust Company of Pennsylvania;

b. Smith W. Bagley;

c. The Northwestern Bank;

d. A. M. Pullen and Company;

e. David R. Johnston

These objections were filed on December 5,

1979.

11. Objections by Shelton-Fulk employee class claimants to the below listed claims:

a. American Bank and Trust Company of Pennsylvania;

b. A.M. Pullen and Company;

c. The Northwestern Bank;

d. David R. Johnston;

e. Smith W. Bagley

These objections were filed on December 5, 1979.

12. Application of American Bank and Trust Company to dismiss objections to its claims by Shelton, et al. and Collins, et al. This application was filed on December 17, 1979.

13. Application by Northwestern Bank to dismiss the objections of its claims by Shelton, et al. and Collins, et

al. This application was filed on December 17, 1979.

14. Motion by David R. Johnston to dismiss the objections to its claim by Shelton, et al. and Collins, et al. This motion was filed on December 18, 1979.

The Collins shareholder class claimants and Shelton-Fulk employees' class claimants are represented by Henry C. Ikenberry, Calvin H. Cobb, Jr., Robert E. McLaughlin, Loren Kieve, John D. Alkire and Howard H. Stahl appearing for the law firm, Steptoe and Johnson, 1250 Connecticut Avenue, N.W., Washington, D. C. 20036. (Hereinafter referred to as "Steptoe.") The Steptoe firm is associated with Blackwell, Blackwell, Canady and Eller, 2100 Wachovia Building, Winston-Salem, North Carolina 27102. (Hereinafter referred to as "Blackwell".) Smith, Anderson, Blount,

Dorsett, Mitchell and Jernigan, Post Office Box 31, Raleigh, North Carolina 27602 represents a subsequently joined party plaintiff, Glen A. Wilkinson.

The Northwestern Bank is represented by Helms, Mulliss & Johnston, 2800 NCNB Plaza, Charlotte, North Carolina 28280.

A.M. Pullen and Company is represented by Nichols, Caffrey, Hill, Evans and Murrelle, Post Office Box 989, Greensboro, North Carolina 27402.

The American Bank and Trust Company of Pennsylvania is represented by Moore and Van Allen, 3000 NCNB Plaza, Charlotte, North Carolina 28280.

The Trustee is represented by C. Edwin Allman, appearing for the law firm of Hatfield and Allman, Post Office Drawer 34, Winston-Salem, North Carolina 27101.

Counsel for the Corporate Reorganization Division of the Securities and Exchange Commission, Rodney May, represented the Securities and Exchange Commission, 1100 L. Street, N.W., Washington D. C. 20005.

David R. Johnston was represented by Wardlow, Knox, Knox, Robinson and Freeman, 1490 City National Center, Charlotte, North Carolina 28202.

All of the matters being decided in this Opinion hinge upon the determination of two central issues:

1. Should the Collins shareholder class claimants be allowed to file a proof of claim in this Chapter X proceeding?
2. Are the Collins shareholder class claimants and Shelton-Fulk

employee class claimants parties in interest for purposes of objecting to claims of creditors filed in this Chapter X proceeding?

In arriving at a solution to these problems, any reference to related actions now pending in the United States District Court for the Middle District of North Carolina will be made only for the purpose of determining the issues in this bankruptcy proceeding. This Opinion is not in any way a comment on or criticism of such actions in the District Court. The facts and conclusions found by this Court are found as a means of reaching justice in the matters pending before this Court.

These complex problems had their origin about eight years ago when a stockholders' class action suit was instituted

in the United States District Court for the Middle District of North Carolina (Civil Action #C-27-WS-73) on January 23, 1973. The full caption follows:

EMIL N. SHAFFNER,
LOUIS deS. SHAFFNER,
JANE FERRELL CLAY,
MOLLY FERRELL REILY,
CAROLINA-TEXAS CORPORATION,
WEBSTER A. COLLINS,
DOUGLAS B. COLLINS,

suing derivatively on behalf of themselves and all other stockholders of the Washington Mills Company and representatively on behalf of themselves and all other shareholders similarly situated,

Plaintiffs,

v.

WASHINGTON GROUP, INC. (formerly the WASHINGTON MILLS COMPANY),
WASHINGTON MILLS-RETAIL, INC.,
SMITH BAGLEY,
JAMES R. GILLEY,
DOUGLAS DILLARD,
JAMES W. FEATHERSTONE, III,
WALSER A. BLACKWOOD,
JOHN D. SIEWERS,
LAWRENCE G. REID,
HENRY M. LESLIE,
GEORGE E. CLAYTON, JR.,

ROBERT H. VAUGHN,
GEORGE W. FULK,
CONVENIENT SYSTEMS, INC.,
WHEAT, FIRST SECURITIES, INC.,

Defendants.

This class action alleged that there was a wrongful merger of Washington Mills-Retail, Inc., a wholly-owned subsidiary of Washington Mills Corporation and Convenient Systems, Inc. Under the terms of the merger agreement, Convenient Systems, Inc., shareholders, surrendered their stock and received one Washington Mills Corporation stock share for each three shares of Convenient Systems, Inc. stock turned in (after a 2:1 split on the Washington Mills Corporation stock). As a result of this merger agreement, Smith Bagley owned 32.5% of the outstanding Washington Mills Corporation stock, and James Gilley, 33.1%. (Smith Bagley and James Gilley later be-

came controlling stockholders and officers in the later created Washington Group, Inc. which was a holding company for Washington Mills Corporation and other subsidiaries.) Washington Mills-Retail, Inc., the newly created subsidiary of Washington Mills Corporation was the vehicle used for the merger. Convenient Systems, Inc., merging with Washington Mills-Retail, Inc. then became merged with Washington Mills Corporation, the parent corporation of Washington Mills-Retail, Inc. The loan of $2,500,000 secured by Convenient Systems, Inc. which was used to finance the purchase of Washington Mills Company stock was then assumed by the Washington Mills-Retail, Inc. As a result of the somewhat complicated merger between Washington Mills-Retail, Inc. and Convenient Systems, Inc., the aforesaid loan

of $2,500,000 became the obligation of the parent corporation Washington Mills Corporation.

This merger arrangement was the subject matter of the Shaffner complaint against Washington Mills Company and the later created Washington Group, Inc. and its officers and directors. This suit was settled out of court before the defendants filed a formal answer to the complaint. The consent judgment settling the issues was entered on August 29, 1973. The settlement provided that dissatisfied stockholders could redeem their stock at $19 a share with a future date for redemption designated or to be designated by the defendants. At the time the suit was instituted, stock was selling for about $14 a share, but by the time the redemption period arrived, the stock had

increased in market value to over $22 a share. As a result, less than $1,600 worth of stock shares were redeemed.

A total of approximately $934,000 was paid in attorneys' fees in connection with the Shaffner suit. Of these fees, approximately $225,000 was paid to Steptoe and Johnson and Blackwell and Blackwell who served as counsel representing the plaintiffs in the Shaffner case. The remaining $709,000 was paid to counsel for the defendants in the Shaffner case. The attorneys' fees for both the plaintiffs and the defendants in Shaffner were paid by Washington Group, Inc.

On June 20, 1977 the Washington Group, Inc. holding company and its totally owned subsidiaries (as listed in the caption of this Opinion) filed these Chapter X bankruptcy proceedings. All of

the proceedings have been combined for administrative purposes by Court Order. The Washington Group employs about 3,000 people. The subsidiaries are principally involved in the manufacture of apparel, manufacture of yarn, operation of sales outlets and operation of a chain of ice cream family dining establishments known as Mayberry. The total assets of Washington Group amounted to approximately $30,000,000 to $40,000,000 at the initiation of these proceedings. The Trustee in these proceedings was directed by the Court pursuant to Section 167 of the Bankruptcy Act to make a thorough investigation of all activities and matters of the corporations and officers including transfer of stock, salaries and bonuses, and possible fraud. This investigation involved depositions of numerous witnesses, documents and other

information totaling over 2,500 pages of testimony. The Trustee filed his Section 167 Investigative Report on June 30, 1978. The report contained approximately 100 pages of condensed facts obtained during the investigation. The Trustee reported that there had been stock price maneuvering and stock price support schemes which influenced the stock value beyond the real value and beyond the price it would normally have been if it had not been financially supported. Also it was reported that there had been mismanagement of the business including mismanagement of the pension plan funds of the employees.

Immediately after this 167 Investigative Report was filed, the Trustee made application to the Court for authority to institute legal actions based on fraud, misconduct, irregularities, or mismanage-

ment of the debtor corporations. This Court entered an Order to this effect on July 25, 1978. Although the application for this Order requested permission to join with other plaintiffs in the prosecution of such claims or causes of actions, the application did not set forth in detail who and how the Trustee was joining with other plaintiffs in order to recover such funds. Pursuant to the July 25, 1978 Order, an action was instituted in the United States District Court for the Middle District of North Carolina styled:

> RICHARD A. GILBERT, Reorganization Trustee of The Washington Group, Inc.,
>
> and
>
> WEBSTER A. COLLINS; DOUGLAS B. COLLINS; HERBERT R. MORRISON; HELEN O. MORRISON; W. O. GREGORY; DR. HORACE H. HICKS; Individually and as representatives of all other similarly situated shareholders of The Washington Group,

Inc. (formerly The Washington Mills Company),

Plaintiffs,

v.

SMITH W. BAGLEY; JAMES L. GILLEY; DAVID R. JOHNSTON; MICHAEL W. RIGGSBEE; THE NORTHWESTERN BANK: DEWEY W. CHAPPLE, JR.; AMERICAN BANK & TRUST CO. OF PA.; WHEAT, FIRST SECURITIES, INC.; INTER-STATE SECURITIES CORP.; WILLIAM F. THOMAS; A. M. PULLEN & CO.,

Defendants, No. C-78-335-WS.

The first 38 pages of the complaint in the Collins shareholders' class action contains allegations pertaining to the fraud involved in the Shaffner case. Almost every page refers to the Shaffner case in which the Washington Group, Inc. was a defendant and paid all the attorneys' fees and costs. The next 12 or 14 pages of the complaint allege causes of action by the Trustee on behalf of Washington Group against certain parties for fraud, mis-

conduct, irregularities and mismanagement of the debtor corporations. The class action alleges a total of approximately $2.2 million in damages and the Trustee is requesting recovery of about $10 million. With the exception of Webster A. Collins and Douglas B. Collins, none of the stockholder plaintiffs in the Shaffner case are plaintiffs in this case. Instead of reopening the Shaffner case and pursuing a cause of action against the officers individually and the debtor corporations, Steptoe and Johnson have elected to pursue a new avenue. In the Collins shareholders' class action which arose out of the Shaffner allegations, Steptoe chose to institute a new action against the former defendant officers individually and joined the former defendant corporation Washington Group, the debtor, as a joint party

plaintiff instead of being a defendant. In the controversy now before the Court, Steptoe has shifted again and now is trying to place the Washington Group in a defendant posture by attempting to file a claim against the debtor corporation. This inconsistency in pursuing the alleged cause of action and election of incompatible alternative remedies troubles this Court and will be discussed later in detail in this Opinion.

In addition to the Collins shareholders' class action, another civil action was instituted in the Federal District Court for the Middle District of North Carolina at the same time by employees alleging mismanagement and irregular manipulations of the Employees' Pension and Profit-Sharing Plans to wit:

GEORGE W. FULK, Chairman of
the Pension, Profit-Sharing,
and Stock Purchase Plan

Committees of the Washington Group, Inc.; and RUBY IRENE LESTER, IRENT TOMLINSON, THOMAS W. SHELTON, WILLIAM F. SUDDETH, suing on behalf of themselves and all other persons similarly situated,

Plaintiffs,

v.

SMITH W. BAGLEY, JAMES R. GILLEY, Individually and as Principal Officers and Members of the Board of Directors of The Washington Group, Inc.; AMERICAN BANK AND TRUST CO. OF PA., A Pennsylvania Corporation; and THE NORTHWESTERN BANK, a North Carolina Corporation,

Defendants., No. C-78-333-WS.

All plaintiffs of this action are present employees of the debtor, The Washington Group, except one. George W. Fulk is the treasurer and an executive officer of the debtor and has been in this position for several years. All of these plaintiffs are under the control and have been under the control of the Trustee

since the debtor corporations filed for reorganization. Steptoe and Blackwell are the attorneys for the plaintiffs in this action as well as the attorneys in the prior Shaffner suit.

The Trustee of the debtor corporations filed an application for authority to aid and assist in the prosecution of legal action based on claims arising out of the administration of the debtor's Profit-Sharing Plan on July 20, 1978. An Order granting authority to aid and assist in the prosecution of legal action based on claims arising out of the administration of the profit-sharing plans was entered on July 21, 1978. Later the Trustee filed a more detailed application to advance expenses for the maintenance of both the Shelton-Fulk employees' class action and the Collins shareholders' class action.

This application of the Trustee was filed on January 15, 1979 and contained the following justification for the debtor corporations financing the civil actions:

> "The successful prosecution of these actions and recovery would negate the necessity of your applicants' having to deal with the employees as claimants within the context of a plan of reorganization."

The application also stated:

> "[M]oreover, many of the employees are shareholders who would benefit from the successful prosecution of the Gilbert v. Bagley action. The assistance and morale of the employees are essential ingredients to any successvul plan of reorganization and to the financial rehabilitation of the debtors. In addition to the obvious uncertainties inherent in any reorganization proceeding, these employees have seen their hard earned employee pension, profit-sharing and stock purchase benefits and investments reduced substantially."

An Order authorizing the expenditure of

funds and costs in these plenary class actions was entered on January 16, 1979. This Order was appealed and later reversed on appeal by the District Court for the Middle District of North Carolina and since has been appealed to the Fourth Circuit. This Court (based on the Trustee's statements) allowed the Trustee to pursue these matters in Federal Court and expend debtor funds in such pursuit to avoid dealing with these large, unliquidated, class claims in the context of reorganization. If the circumstances and facts concerning these suits now known to this Court had been known at the time application for authority to expend funds for costs in these plenary class actions was made, this Court would have never entered the January 16, 1979 Order allowing such expenditures.

A list of creditors and stockholders of the corporate debtor was filed by the Trustee on August 19, 1977. This list does not contain the claims which are now alleged in the Shelton-Fulk employees' class action and the claims in the Collins shareholders' class action. The first bar date Order for filing claims was entered by this Court on February 9, 1978 requiring all creditors to file a proof of claim by February 24, 1978. A notice of this Order was not officially sent to stockholders and employees but was sent to all known potential creditors. However, all employees with the corporation and all stockholders knew or should have known that Washington Group was in a Chapter X proceeding and had been in such for some time. The proceeding was well publicized through notices, employee newsletters, news items and other news mediums.

On the 27th day of August, 1979, upon application of the Trustee, a supplementing Order was entered by this Court directing those creditors who were listed on the list of creditors and who had not filed a proof of claim as of the date of that Order, to file such on or before October 8, 1979. Another bar date Order was entered on June 20, 1977, upon the request of the Trustee and at the insistence of the attorney for the proposed purchaser of The Washington Group stock pursuant to a plan of reorganization then pending before this Court. The June 20 Order directed all potential creditors, wherever located, to file proofs of claim or be forever barred. This Order was entered only to protect the prospective purchaser in the proposed reorganization plan from potential creditors who may not have received actual notice of

the pending proceedings and bar date Orders. This Order was not intended to be a blanket extension for all parties who had prior to that time received actual notice of such, but was intended only as a newspaper publication notice to the entire world. Parties such as the Collins shareholder class claimants and Shelton-Fulk employee class claimants were not covered under this Order, because they had prior to this date received actual notice of the pending proceedings and effective bar dates. Steptoe and Johnson through their representative, Mr. Stahl, represented to this Court that they became aware of the potential claims as early as June 30, 1978 when the Section 167 Trustee's Investigative Report was filed with this Court. In addition, Steptoe and Johnson had to have been aware of the potential claim by

virtue of their involvement in the prior Shaffner litigation which the new cases are based upon. In spite of this, Steptoe and Johnson and Blackwell and Blackwell filed no proofs of claims, applications or any other matters on behalf of their clients in this Court until the 14th day of September, 1979, which was by coincidence one day before the hearing on the proposed plan of reorganization. The true facts are that Steptoe and Blackwell had no intention of filing a proof of claim in the Bankruptcy Court prior to that time and changed course merely because they were experiencing difficulty with class certification in Federal Court and a successful sale and plan of reorganization seemed imminent in Bankruptcy Court. This plan of reorganization does not recognize nor treat the Collins and Shelton-Fulk

claimants. Steptoe and Blackwell were aware of this for some time, but did not file proofs of claims until the eve of the hearing on the proposed plan. This new development made The Washington Group a defendant in Bankruptcy Court and a joint plaintiff in Federal District Court at the same time and arising out of the same matter. The filing of the proofs of claims on September 14, 1979 was the beginning of an "avalanche" of filings by Steptoe and Johnson and Blackwell and Blackwell in this bankruptcy proceeding. The filings since that date have been as follows:

1.	9-14-79	Applic. by Collins, et al. to amend Tr.'s list of creditors	1F-220 2 pgs.
2.	9-14-79	Applic. by Shelton, et al. to amend Tr.'s list of creditors	1F-221 2 pgs.
3.	9-14-79	Objection to	63F/O-213 2 pgs.

		Plan by Shelton, et al.		
4.	9-14-79	Supplement to objection to Plan by Collins, et al.	63F-249	2 pgs.
5.	9-14-79	Statement required by Rule 10-211 by Collins, et al.	63F/O-215	5 pgs.
6.	9-14-79	Supplement to objection to Plan by Shelton, et al.	63F-250	2 pgs.
7.	9-14-79	Objection to Plan by Collins, et al.	63F/O-217	2 pgs.
8.	10-17-79	Supplemental Statement of Representatives	63F-231	3 pgs.
9.	10-23-79	Pre-hearing Brief of Shelton, et al. in support of their applications to list of creditors	1F-236	16 pgs.
10.	10-23-79	Brief of claimants, Collins, et al. in support of their applications to amend list of creditors	1F-237	16 pgs.
11.	11-02-79	Supplement to application to	1F-245	3 pgs.

		amend list of creditors by Shelton, et al.		
12.	11-02-79	Supplement to application to amend list of creditors by Collins, et al.	1F-246	3 pgs.
13.	12-04-79	Reply Brief of applicants Shelton, et al. in support of their applications to amend list of creditors	1F-258	125pgs.
14.	12-04-79	Reply Brief of applicants Collins, et al. in support of their applications to amend list of creditors	1F-259	43 pgs.
15.	12-05-79	Objection to Confirmation of Plan by Shelton, et al.	63F/O-261	8 pgs.
16.	12-05-79	Objection to Confirmation of Plan by Collins, et al.	63F/O-264	8 pgs.
17.	12-05-79	Objections by Collins et al. to the below listed claims:		

	1. American Bank & Trust Co. of Pa.	53F-265	2 pgs.
	2. Smith W. Bagley	53F-266	2 pgs.
	3. The North-western Bank	53F-267	3 pgs.
	4. A.M. Pullen & Co.	53F-269	3 pgs.
	5. David R. Johnston	53F-268	3 pgs.
18. 12-05-79	Objections by Shelton, et al. to the below listed claims:		
	1. American Bank & Trust Co. of Pa.	53F-270	2 pgs.
	2. A.M. Pullen & Co.	53F-271	2 pgs.
	3. The North-western Bank	53F-272	2 pgs.
	4. David R. Johnston	53F-273	2 pgs.
	5. Smith W. Bagley	53F-274	2 pgs.
19. 12-11-79	Supplemental request by Collins, et	53F-285	8 pgs.

		al. for temporary allowance of claim for purpose of accepting or rejecting Plan		
20.	12-11-79	Supplemental request by Shelton, et al. for temporary allowance of claim for purpose of accepting or rejecting Plan	53F-286	3 pgs.
21.	1-15-80	Letter from Stahl of Steptoe & Johnson; re: substantial pleadings in representation of Collins, et al. and Shelton, et al.	53F-362	
22.	3-10-80	Descriptive index to briefs & matters filed on behalf of Collins & Shelton, et al.		4 pgs.
23.	3-10-80	Desig, of record relevant to issues identified by the Court		6 pgs.

24.	3-17-80	Written statement by Shelton, Suddeth & Fulk of grounds for objection to secured status of American Bank & Trust Co.	53F-400	6 pgs.
25.	3-17-80	Written statement by Collins, et al. of grounds for objection to secured status of American Bank & Trust Co.	53F-401	6 pgs.
26.	4-14-80	Comprehensive posthearing reply brief by Shelton, et al.	c/53F-412	49 pgs.
27.	4-14-80	Comprehensive posthearing reply brief by Collins, et al.	c/53F-411	49 pgs.

In addition to the above 27 filings consisting of a total of 392 pages, Steptoe has presented to this Court hundreds of other pages of material relating to but not filed in this proceeding. In open Court Steptoe indicated that already

the legal fees in connection with lawsuits in the District Court and the Bankruptcy Court so far would amount to $750,000 to $1,000,000. (As of the date of this Opinion, both class actions brought by Steptoe and Blackwell have not been certified in the United States District Court as class actions.) The Steptoe and Blackwell attorneys have attended 10 to 12 days of hearing in this Court on the plan and the confirmation of the plan as hereinabove mentioned as well as two or three appearances on the matters being decided in this Opinion. After hearing Steptoe in Court and considering all documents filed and presented to this Court for consideration, it is the conclusion of this Court that the so-called class claims and actions by Collins and Shelton-Fulk which are the basis of the alleged claims before this

Court are being pursued for the benefit of the attorneys rather than for the benefit of their so-called plaintiffs and clients. Many of these filings are considered by this Court to be frivilous and certainly not necessary or appropriate to promote and benefit the cause of their clients. Furthermore, it is the conclusion of this Court that the named representative class claimants are no more than "straw claimants" and these claims are made on behalf of the attorneys, not a valid, certifiable group of class claimants.

A question of conflict of interest has also been raised as to whether the Steptoe law firm's representation of the two different and competing class claimants is a conflict of interest in these bankruptcy proceedings. Since the applications and

class claims are being denied by this Court, it is not necessary to make a determination on that question at this time.

It is found by this Court that it would be unfair, inequitable and unjust to allow the Collins shareholders' class claim and the Shelton-Fulk employees' class claim to be filed against the debtor estate for the following reasons:

1. Fraud was alleged in the 1977 stockholder class action (Shaffner) which these class claims are based on. The normal procedure would have been to file a claim against the debtor corporation and ask that the prior settled case be re-opened and the matter liquidated in the District Court. This would have made the debtor corporation a defendant. (Steptoe and Blackwell were the attorneys in this

1973 suit in which they received a fee of $250,000.) However, instead of making the debtor a party defendant, Steptoe "made friends" with and co-plaintiffs of the debtor and Trustee for the sole purpose of gaining benefits and aid from the debtor and Trustee by access to debtor files and information. Steptoe benefited from the co-plaintiff relationship as follows:

a. The costs in the Collins shareholder class action (in which the Trustee was a co-plaintiff) was being furnished by the Trustee on behalf of the debtor.

b. The cost of the Shelton-Fulk employee class action was provided by the Trustee, pursuant to Court Order even though the plaintiff was not a party. However, such approval by the Court has since been reversed. (See above.)

c. Most importantly, clients or party plaintiffs were furnished by the Trustee to Steptoe and Blackwell in both cases, especially the pension suit. All plaintiffs, except one, in the pension suit are employees of the debtor corporation.

d. Steptoe and Blackwell by joining the Trustee as co-plaintiff had access to all information, goodwill, and other advantages which the former defendant corporation, now plaintiff, could give.

2. The plaintiff's action for mismanagement of the corporation by former officers has been taken over and is now being controlled by Steptoe and Blackwell by reason of the joint lawsuit. In the Collins suit, the Trustee is claiming actual damages of approximately $10,000,000 on other grounds while the attorneys in control of the suit are asking for

$10,000,000 in actual damages arising out of claims asserted in the former Shaffner suit. In other words, Steptoe has taken over the civil lawsuits from the Trustee for all practical purposes.

It is clear to this Court that Steptoe and Blackwell are now attempting to turn against the Trustee and "bite the hand that financed them." Steptoe has now turned against the Trustee, co-plaintiff in the pending litigation in District Court, and made the Trustee a defendant now in the bankruptcy proceedings based on the exact same claim. In fact, the Trustee has been "boxed-in" by this recent development. It is difficult for the Trustee to deny that there is not a valid claim against the estate when at the same time he is contending that the directors, officers, and other parties who in the past represented

the debtor corporation are in fact liable. It is conceivable that this is the reason the Trustee filed a "feeble" reply to the applications filed by Steptoe for listing and recognition as class claimants in the bankruptcy proceeding.

In August, 1979 the Trustee filed a plan of reorganization in which an outside company would become the stockholder and owner of all the Washington Group subsidiaries except Mayberry. Extensive hearings were had on the plan before it was finally approved by this Court. The plan was submitted to creditors and stockholders for voting but was rejected by a sufficient number of stockholders. During these hearings it appeared that the stockholder equity was very "thin". In fact, the stockholder equity, without the consideration of the two class claims as

herein mentioned and without recognizing about $1,000,000 in other contested claims, would be less than $3,000,000. If these two class claims were to be recognized and were to be liquidated as class action claims, the estate would be insolvent. In order to comply with the strict priority rule there will have to be a determination of solvency which would require a liquidation of these claims, if allowed, before a plan could be filed again. Due to economic conditions and especially the present business conditions of these companies, it is imperative that a plan be formulated and presented in the near future. It would not be feasible to delay presentation of a plan for possibly years in order to have a determination of class claims of this type. The rights and benefits of other creditors, including

existing stockholders, should not be jeopardized by diliatory actions and the selection of a wrong remedy by Steptoe. Steptoe, on behalf of its class clients, elected to pursue a remedy in Federal District Court whereby the corporation through its representative, the Trustee, was joined as a co-plaintiff. The theory of the election to sue the officers individually and join the debtor as a co-plaintiff is that the officers and directors were acting outside of their scope of employment and responsibilities as officers and directors. Steptoe (on behalf of its clients) cannot now come into Bankruptcy Court and choose a completely inconsistent remedy by now seeking to made the co-plaintiff in District Court a defendant in Bankruptcy Court. The theory of proceeding in Bankruptcy Court

and making the debtor corporation a defendant along with the officers and directors is that the officers and directors in fact acted within their scope of employment as officers. The class claimants should not be allowed to pursue both theories at the same time in different Courts because these two avenues of remedy are entirely inconsistent.

Under considerations of fair play and equity, both applications to become listed class creditors and be recognized as class claimants should be denied. The Bankruptcy Act deals with classes of creditors but not class action claims. There are no provisions for class actions and filing of class claims in the Bankruptcy Court under the Bankruptcy Act. Even if there were such provisions, these class groups have already chosen their avenue and should not

be allowed at this time to file and thus delay any feasible plan for years to come. The cost to the debtor would be astronomical and totally unfeasible.

Steptoe and Blackwell under the names of the Collins and Shelton-Fulk parties have also filed objections to the allowance of the claims of American Bank & Trust Company of Pa., A. M. Pullen & Co., The Northwestern Bank, David R. Johnston, and Smith W. Bagley in this Court. These creditors are already defendants in the Steptoe cases as now pending in the United States District Court. Since the Steptoe and Blackwell clients are not recognized as creditors or stockholders in these proceedings, they have no standing to object to these creditors' claims and such objections should be dismissed.

Let an Order be entered pursuant to this Memorandum Opinion denying the application and claims of the parties and dismissing the objections to the claims for reasons herein stated.

This the 15th day of May, 1980.

RUFUS W. REYNOLDS
U. S. BANKRUPTCY JUDGE

APPENDIX B

29 U.S.C. §1031 provides:

Repeal and effective date

(a)(1) The Welfare and Pension Plans Disclosure Act is repealed except that such Act shall continue to apply to any conduct and events which occurred before the effective date of this part.

(2)(A) Section 664 of Title 18 is amended by striking out "any such plan subject to the provisions of the Welfare and Pension Plans Disclosure Act" and inserting in lieu thereof "any employee benefit plan subject to any provision of title I of the Employee Retirement Income Security Act of 1974".

(B)(i) Section 1027 of such Title 18 is amended by striking out "Welfare and Pension Plans Disclosure Act" and inserting in lieu thereof "title I of

the Employee Retirement Income Security Act of 1974", and by striking out "Act" each place it appears and inserting in lieu thereof "title".

(ii) The heading for such section is amended by striking out "Welfare and Pension Plans Disclosure Act" and inserting in lieu thereof "Employee Retirement Income Security Act of 1974".

(iii) The table of sections of chapter 47 of such Title 18 is amended by striking out "Welfare and Pension Plans Disclosure Act" in the item relating to section 1027 and inserting in lieu thereof "Employee Retirement Income Security Act of 1974".

(C) Section 1954 of such Title 18 is amended by striking out "any plan subject to the provisions of the Welfare and Pension Plans Disclosure Act as

amended" and inserting in lieu thereof "any employee welfare benefit plan or employee pension benefit plan, respectively, subject to any provision of title I of the Employee Retirement Income Security Act of 1974"; and by striking out "sections 3(3) and 5(b)(1) and (2) of the Welfare and Pension Plans Disclosure Act, as amended" and inserting in lieu thereof "sections 3(4) and (3)(16) of the Employee Retirement Income Security Act of 1974".

(D) Section 211 of the Labor-Management Reporting and Disclosure Act of 1959 (section 441 of this title) is amended by striking out "Welfare and Pension Plans Disclosure Act" and inserting in lieu thereof "Employee Retirement Income Security Act of 1974".

(b)(1) Except as provided in paragraph (2), this part (including the amendments and repeals made by subsection (a) of this section) shall take effect on January 1, 1975.

(2) In the case of a plan which has a plan year which begins before January 1, 1975, and ends after December 31, 1974, the Secretary may postpone by regulation the effective date of the repeal of any provision of the Welfare and Pension Plans Disclosure Act (and of any amendment made by subsection (a)(2) of this section) and the effective date of any provision of this part, until the beginning of the first plan year of such plan which begins after January 1, 1975.

(c) The provisions of this subchapter authorizing the Secretary to promulgate regulations shall take effect on September 2, 1974.

* * * *

29 U.S.C. §1137(b) provides:

No employee of the Department of Labor or the Department of the Treasury shall administer or enforce this subchapter or the Internal Revenue Code of 1954 with respect to any employee benefit plan under which he is a participant or beneficiary, any employee organization of which he is a member, or any employer organization in which he has an interest. This subsection does not apply to an employee benefit plan which covers only employees of the United States.

* * * *

29 U.S.C. §1144(d) provides:

Nothing in this subchapter shall be construed to alter, amend, modify, invalidate, impair, or supersede any law of the United States (except as provided

in sections 1031 and 1137(b) of this title) or any rule or regulation issued under any such law.